

Management's Discussion and Analysis

MANAGEMENT'S DISCUSSION AND ANALYSIS

The City of Seattle (City) presents this Management's Discussion and Analysis (MD&A) of its financial activities for the fiscal year ended December 31, 2004. This discussion and analysis focuses on significant financial issues, provides an overview of the City's financial activity, highlights significant changes in the City's financial position, and identifies material variances between the approved budget and actual spending.

The City encourages readers to consider the information presented here in conjunction with additional information provided in its letter of transmittal.

FINANCIAL HIGHLIGHTS

- At the end of fiscal year 2004 the assets of the City of Seattle exceeded its liabilities by \$2.685 billion. Net assets invested in capital assets (net of depreciation and related debt) account for 84.2 percent of this amount (\$2.261 billion). The remaining net assets of \$424.3 million may be used to meet the City's ongoing obligations to citizens and creditors.
- The City's net assets increased by \$142.2 million (5.6 percent) during the fiscal year. The governmental net assets increased by \$117.5 million (6.8 percent) over the amount reported in 2003. Business-type net assets increased by \$24.7 million (3.0 percent). The business-type increase included net income for the Water Utility of \$17.8 million and \$13.8 million for City Light, reduced by a net loss of \$5.0 million for the Drainage and Wastewater Utility and losses of \$1.4 million in the nonmajor funds. The balance of the offset is the result of the consolidation of the Internal Service Funds' activities related to the Enterprise Funds.
- At the close of 2004 the City's governmental funds reported a combined ending fund balance of \$332.6 million, a decrease of \$47.3 million (12.5 percent). The fund balance of the General Fund increased \$13.4 million and the fund balance of the Low-Income Housing Fund increased by \$8.7 million. The fund balances of the debt service funds increased by \$2.0 million while the fund balances of the remaining special revenue funds and the capital projects funds decreased by \$8.7 million and \$62.5 million, respectively. The decreases were largely due to the planned spend-down of fund balances in the special revenue funds as well as the spend-down of cash in the capital projects funds as construction continued or was completed on major governmental projects, such as the Central Library. Approximately \$55.9 million (16.8 percent) of the combined ending fund balance is unreserved fund balance available to the City for discretionary spending.
- At the end of 2004 the unreserved fund balance for the General Fund was \$40.7 million or 8.0 percent of total General Fund expenditures of \$509.4 million. The General Fund's unreserved fund balance decreased by approximately \$1.6 million from the prior year's amount of \$42.2 million, a 3.7 percent change. This change is largely attributed to the shift in funding of the City's streetlights from Seattle City Light to the General Fund.
- The City's total outstanding bonded debt increased by \$82.0 million (2.3 percent) during the current fiscal year to \$3.574 billion. Revenue bonds and anticipation notes increased by \$133.7 million. The increase included \$15.7 million for City Light, \$63.2 million for Water, and \$56.8 million for Drainage and Wastewater. This was offset by a decrease of \$2.0 million for Solid Waste. General obligation debt decreased by \$51.7 million in 2004. Key factors in the decrease were the defeasance and payoff of the 1994 Seattle Center Coliseum bonds, the 2004 refunding bond issue, and the principal payments on other bonds.
- Revenues from local tax sources including property, sales, business excise, miscellaneous other taxes, penalties and interest on taxes, increased by \$48.3 million to \$715.0 million, a 7.2 percent increase over 2003. Unrestricted investment earnings dropped by 37.8 percent from \$15.5 million to \$9.6 million. The decrease was due to two factors: the continued low interest rates coupled with the reduction in cash balances in the capital projects funds.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is an introduction to the City of Seattle's basic financial statements which consist of three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the financial statements. The report also contains other supplementary information in addition to the basic financial statements.

Government-Wide Financial Statements

The government-wide financial statements provide a broad overview of the City's finances in a manner similar to that of private-sector business.

The **statement of net assets** presents information on all City assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of the City's financial health.

The **statement of activities** presents changes in net assets during the current reporting period. All changes to net assets are reported as of the date of the underlying event, rather than when cash is received or disbursed. Thus, some reported revenues and expenses result in cash flows in future periods. The statement of activities focuses on both the gross and net cost of the various activities of the City. The report summarizes and simplifies analysis of the revenues and expenses of the various City activities and the degree to which activities are subsidized by general revenues.

The government-wide financial statements distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that recover all or a significant portion of their costs through user fees and charges (business-type activities). The governmental activities of the City include general government activities, judicial activities, public safety, physical environment, transportation, economic environment, health and human services, and culture and recreation. The business-type activities of the City include an electric utility, a water utility, a waste disposal utility, a sewer and drainage utility, construction and land use operations, and parking facilities.

Fund Financial Statements

A fund is a group of related accounts used to maintain control over resources that are segregated for specific activities or objectives. The City, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. There are three categories of City funds: **governmental** funds, **proprietary** funds, and **fiduciary** funds.

Governmental funds account for essentially the same functions reported as governmental activities in the government-wide financial statements. Most of the City's basic services are reported in the governmental funds. These statements, however, focus on cash and other assets that can readily be converted to available resources, as well as any balances remaining at year-end. Such information is useful in determining what financial resources are available in the near future to finance the City's programs.

Readers may better understand the long-term impact of the government's near-term financing decisions by comparing the information presented for the governmental funds with similar information presented for governmental activities in the government-wide financial statements. Both the governmental funds balance sheet and the governmental funds statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate the comparison.

The City maintains numerous governmental funds that are organized according to type (general, special revenue, debt service, capital projects, and permanent funds). Information for the two major governmental funds is presented separately in the governmental funds balance sheet and in the governmental funds statement of revenues, expenditures, and changes in fund balances; information for the nonmajor funds is presented in the aggregate. The City's major governmental funds are the General Fund and the Low-Income Housing Fund. Information for each of the nonmajor governmental funds is provided in the combining statements in this report.

Proprietary funds account for services for which the City charges outside customers and internal City departments. Proprietary funds provide the same information as shown in the government-wide financial statements, only in more detail. The City maintains the following two types of proprietary funds:

- **Enterprise funds** report the same functions presented as business-type activities in the government-wide financial statements. The proprietary funds financial statements provide separate information for the Seattle City Light Fund, Water Fund, and the Drainage and Wastewater Fund, which are considered to be major enterprise funds. Information for nonmajor enterprise funds is presented in the aggregate. Information for each of the nonmajor enterprise funds is provided in the combining statements in this report.
- **Internal service funds** report activities that provide supplies and services for various City programs and activities. The City uses internal service funds to account for its fleets and facilities services, information technology services, and engineering services. Because these services largely benefit governmental rather than business-type functions, they have been included within the governmental activities in the government-wide financial statements. The internal service funds are combined into a single aggregated presentation in the proprietary funds financial statements. Information for each of the internal service funds is provided in the combining statements in this report.

Proprietary funds statements follow the governmental funds statements in this report.

Fiduciary funds account for resources held for the benefit of parties outside the government. Fiduciary funds are not reflected in the government-wide financial statements because the resources of these funds are not available to support City programs. The accounting used for fiduciary funds is similar to that used for proprietary funds. The City's fiduciary funds

include the Employees' Retirement Fund, the Firemen's Pension Fund, the Police Relief and Pension Fund, the S. L. Denny Private-Purpose Trust Fund, and various agency funds.

Notes to the Financial Statements

The notes to the financial statements are an integral part of the financial statements. They provide additional disclosures that are essential to a full understanding of the information provided in the government-wide and fund financial statements. The notes to the financial statements immediately follow the basic financial statements in this report.

Required Supplementary Information

This report also contains other required supplementary information (RSI) on budgetary comparisons for major governmental funds and pension plan funding.

Combining Statements

The combining statements referred to earlier in connection with the nonmajor funds, internal service funds, and fiduciary funds are presented immediately following the required supplementary information.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

This is the third year that the City has presented its financial statements under the new reporting model required by the Governmental Accounting Standards Board Statement No. 34 (GASB 34), *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Financial information for the past two years in the GASB 34 format is presented below.

Statement of Net Assets

Table A-1 **CONDENSED STATEMENT OF NET ASSETS**
(In Thousands)

	Governmental Activities		Business-Type Activities		Total	
	2004	Restated 2003	2004	2003	2004	Restated 2003
Current and Other Assets	\$ 806,137	\$ 867,167	\$ 963,300	\$ 838,799	\$ 1,769,437	\$ 1,705,966
Capital Assets and Construction in Progress, Net of Accumulated Depreciation	2,385,606	2,260,807	2,945,448	2,881,747	5,331,054	5,142,554
Total Assets	3,191,743	3,127,974	3,908,748	3,720,546	7,100,491	6,848,520
Current Liabilities	241,375	230,665	293,909	251,066	535,284	481,731
Noncurrent Liabilities	1,111,868	1,176,303	2,768,411	2,647,751	3,880,279	3,824,054
Total Liabilities	1,353,243	1,406,968	3,062,320	2,898,817	4,415,563	4,305,785
Net Assets						
Invested in Capital Assets, Net of Related Debt	1,603,090	1,454,419	657,531	676,051	2,260,621	2,130,470
Restricted	101,326	126,508	98,074	178,897	199,400	305,405
Unrestricted (Deficit)	134,084	140,079	90,823	(33,219)	224,907	106,860
Total Net Assets	\$ 1,838,500	\$ 1,721,006	\$ 846,428	\$ 821,729	\$ 2,684,928	\$ 2,542,735

As noted earlier, net assets may serve as a useful indicator of a government's financial position. Table A-1 is a condensed version of the statement of net assets for the City of Seattle. At the close of the current fiscal year the City's total assets exceeded liabilities by \$2.685 billion.

The largest portion of the City's net assets (84.2 percent) reflects investment of \$2.261 billion in capital assets such as land, buildings, and equipment, less any related outstanding debt used to acquire those assets. The City uses these capital assets to provide services to citizens; consequently, these assets are not available for future spending. Although the City's investment in its capital assets is reported net of related debt, the resources needed to repay the debt must be provided from other sources, as capital assets cannot be used to liquidate these liabilities.

An additional portion of the City's net assets, \$199.4 million (7.4 percent), represents resources that are subject to restrictions on how they may be used. The remaining balance of unrestricted net assets, \$224.9 million (8.4 percent), may be used to meet the government's obligation to citizens and creditors.

In 2004 unrestricted net assets for governmental activities decreased by 4.3 percent from \$140.1 million in 2003 to \$134.1 million in 2004. The City's economic recovery from the previous year's recession boosted the total net assets; however, the decrease in unrestricted net assets is the result of a significant increase in net assets invested in capital, net of related debt and restricted net assets for governmental activities.

The unrestricted net assets for the business activities improved significantly between 2003 and 2004 from a deficit of \$33.2 million to a positive balance of \$90.8 million. The considerable increase in net assets is in part due to the Water Utility's rate increase and City Light's sale of energy to retail customers.

Table A-2

**CHANGES IN NET ASSETS RESULTING FROM
CHANGES IN REVENUES AND EXPENSES
(In Thousands)**

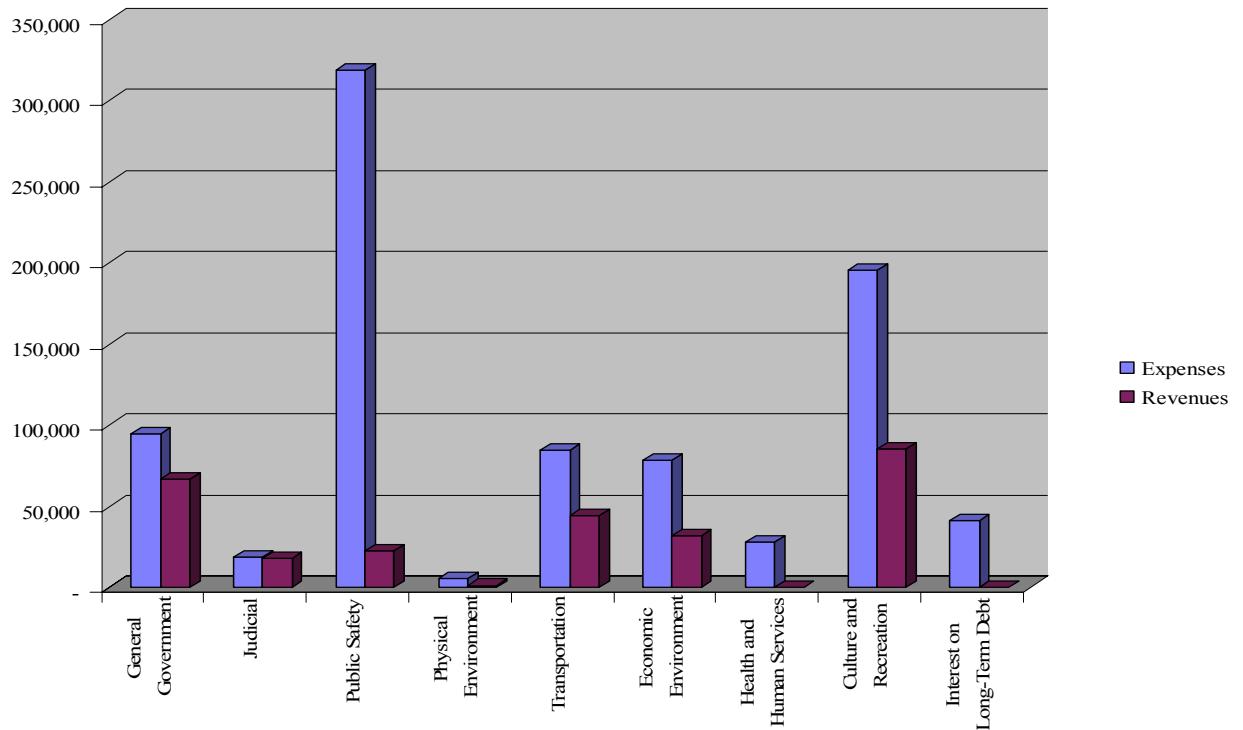
	Governmental Activities		Business-Type Activities		Total	
	2004	Restated 2003	2004	2003	2004	Restated 2003
Revenues						
Program Revenues						
Charges for Services	\$ 152,427	\$ 145,037	\$ 1,221,002	\$ 1,166,768	\$ 1,373,429	\$ 1,311,805
Operating Grants and Contributions	63,512	59,468	2,618	667	66,130	60,135
Capital Grants and Contributions	55,051	37,007	21,014	31,493	76,065	68,500
General Revenues						
Property Taxes	280,460	252,702	-	-	280,460	252,702
Sales Taxes	130,961	124,951	-	-	130,961	124,951
Business Taxes	253,733	248,467	-	-	253,733	248,467
Other Taxes	49,903	40,591	-	-	49,903	40,591
Other	7,662	13,693	6,369	13,583	14,031	27,276
Total Revenues	993,709	921,916	1,251,003	1,212,511	2,244,712	2,134,427
Expenses						
Governmental Activities						
General Government	94,917	101,322	-	-	94,917	101,322
Judicial	19,137	19,211	-	-	19,137	19,211
Public Safety	318,706	298,120	-	-	318,706	298,120
Physical Environment	5,530	5,513	-	-	5,530	5,513
Transportation	84,390	92,749	-	-	84,390	92,749
Economic Environment	78,455	85,130	-	-	78,455	85,130
Health and Human Services	28,145	29,483	-	-	28,145	29,483
Culture and Recreation	195,699	164,488	-	-	195,699	164,488
Interest on Long-Term Debt	41,499	43,216	-	-	41,499	43,216
Business-Type Activities						
Light	-	-	772,827	777,631	772,827	777,631
Water	-	-	127,865	124,611	127,865	124,611
Drainage and Wastewater	-	-	168,689	156,786	168,689	156,786
Solid Waste	-	-	112,920	112,114	112,920	112,114
Planning and Development	-	-	45,320	37,114	45,320	37,114
Downtown Parking Garage	-	-	8,421	8,284	8,421	8,284
Total Expenses	866,478	839,232	1,236,042	1,216,540	2,102,520	2,055,772
Excess (Deficiency) Before Transfers	127,231	82,684	14,961	(4,029)	142,192	78,655
Transfers	(9,738)	(9,569)	9,738	9,569	-	-
Increase in Net Assets	117,493	73,115	24,699	5,540	142,192	78,655
Net Assets - Beginning of Year	1,721,007	1,647,892	821,729	816,189	2,542,736	2,464,081
Nets Assets - End of Year	\$ 1,838,500	\$ 1,721,007	\$ 846,428	\$ 821,729	\$ 2,684,928	\$ 2,542,736

Analysis of Changes in Net Assets

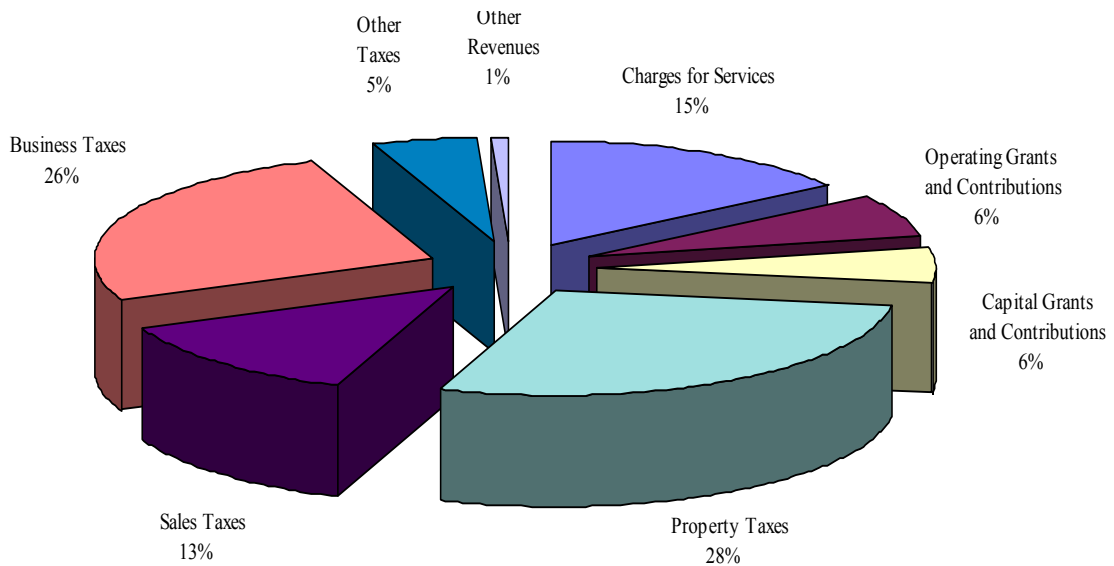
The City's total net assets increased by \$142.2 million in 2004. The increase is explained in the following discussion of governmental and business-type activities.

Governmental Activities

EXPENSES AND PROGRAM REVENUES - GOVERNMENTAL ACTIVITIES



REVENUES BY SOURCE - GOVERNMENTAL ACTIVITIES



Total \$993.7 Million

Governmental Activities. The charts on the previous page present the City's governmental expenses and revenues by function and its revenue by source. Public safety is the largest governmental expense of the City, followed by culture and recreation, general government, transportation, economic environment, health and human services, judicial, and physical environment. General revenues such as the property, business, and sales taxes are not shown by function because they are used to support citywide program activities. Governmental activities increased the City's net assets by \$117.5 million compared to an increase of \$73.1 million in 2003. Key factors in the change are as follows:

In 2004 total revenues for governmental activities were \$993.7 million, \$71.8 million or 7.8 percent higher than 2003.

Program revenue related to charges for services, which includes licenses and permits, fines and forfeits, and other service fees, increased by \$7.4 million in 2004. The 2004 adopted budget included increases to existing fees and fines as well as the creation of some new fees. In 2004 the City collected \$1.8 million from the new police alarm monitoring license and the related new false alarm fee. Parking ticket revenues increased by \$2.2 million as a result of several actions: improved staffing and expanded schedules; a change in collection agencies; and implementation of an amnesty program. In 2004 the revenue from parking meter collections increased by \$1.3 million. The City began installing parking pay stations in 2004. Additional pay stations will be installed in 2005 and 2006. Rates were increased from \$1.00 to \$1.50 as the pay stations were being deployed.

Grants and contributions increased by \$22 million compared to 2003. Capital grants and contributions went up by \$18.0 million. In 2004 the Library received \$26.5 million in donations, up \$18.2 million compared to 2003. Of the \$26.5 million, the Library Foundation contributed \$21.5 million. Operating grants and contributions increased by \$4.0 million, mainly due to federal grants related to the Urban Area Security Initiative programs funded by the Department of Homeland Security.

Property taxes, the largest source of revenue supporting governmental activities increased by \$27.8 million or 11.0 percent compared to 2003. Property tax is levied primarily on real estate owned by individuals and businesses. In 2004 the total property tax rate in Seattle was about 1.04 percent of assessed value. The City's General Fund receives 65 percent of the property tax revenue. In addition, several voter-approved levies support various City programs and projects. In November 2003 Seattle voters approved additional property taxes to finance the building and renovation of fire stations. Collections for the \$167 million fire levy began in 2004 with the City receiving in excess of \$24.4 million. The levy continues until 2012.

The retail sales and use (sales) tax is imposed on the sale of most goods and certain services in Seattle. The tax is collected and remitted to the state. The state provides the City with its share on a monthly basis. After a three-year decline reflecting the severe local recession, with the economy improving in 2004, the sales tax revenues increased by \$6.0 million or 4.8 percent.

Business taxes are the second largest contributor to governmental revenues. The business and occupation (B&O) tax, the major business tax, is levied by the City on the gross receipts of most business activity occurring in Seattle. The City also levies a B&O tax on the gross income derived from sales of utility services within Seattle. In 2004 business tax revenues increased by \$5.3 million or 2.1 percent.

Other tax revenues increased by \$9.3 million or 22.9 percent. The major contributor to the increase was the revenue from the real estate excise tax which was up \$10.7 million due to the strong housing market. This increase was offset by a falloff in revenue from audit activity and penalty and interest payments, down \$2.2 million.

Due to falling interest rates, investment earnings declined by approximately \$4.0 million, from \$9.4 million in 2003 to \$5.4 million in 2004. The average rate of return declined from 3.2 percent in 2003 to 2.3 percent in 2004. Revenue from the sale of capital assets also declined, down \$2.0 million.

In 2004 total expenses for governmental activities were \$866.5 million compared to \$839.2 million in 2003, \$27.2 million or 3.2 percent higher than 2003.

General government expenses were down \$6.4 million compared to 2003. Several items contributed to the decline. Due to the State Supreme Court's ruling that the City's practice of having the Light Fund pay for streetlights was unconstitutional, the 2004 adopted budget was amended in March. To cover part of the annual cost of operating the streetlights, there were across-the-board expenditure cuts for the general government departments. Earthquake repair work continued into 2004 but the amount spent in 2004 was about \$6 million less than in 2003. The Judgment Claims subfund spending was down in 2004; however, these costs were offset by an increase in the liabilities for workers' compensation and judgment and claims at year-end.

The decrease in judicial expenses of \$0.1 million were also the result of the across-the-board expenditure cuts that were made to address the shift in funding of the streetlight costs to the General Fund.

Public safety expenses increased by \$20.6 million, a 6.9 percent increase over 2003. The increase is attributed to three main reasons: (1) receipt of grants by the Police Department and the Fire Departments from the Department of Homeland

Security under the Urban Areas Security Initiative (UASI) Program to combat the increased threat of terrorism; (2) the hiring of additional staff by both departments to provide security for Sound Transit construction and to administer the contract for deployment of life-support transport vehicles; and (3) increased costs of \$4.7 million for workers' compensation and judgment and claims.

Physical environment expenses remained relatively constant in 2004, up 0.3 percent to \$5.5 million.

Transportation expenses decreased by \$8.4 million in 2004. Due to a preliminary court ruling the City recorded a one-time expense of \$23.9 million in 2003, representing a liability for a streetlight refund to electric utility ratepayers. In 2004 the City began paying approximately \$6.2 million to cover the annual cost of operating the streetlights. In 2004 the Seattle Department of Transportation (SDOT) began a 3-year program to install 1,650 pay stations to replace a majority of the City's single space parking meters. During 2004 approximately 500 of the pay stations were installed at a cost of \$2.1 million. In 2004, SDOT was also working on an initiative to manage the City's right-of-way to promote mobility. Transfers from the Seattle Public Utilities and the Department of Planning and Development occurred as a part of the initiative. The department also spent about \$1.0 million on the Monorail plan review. Workers' compensation and judgment and claims costs associated with the transportation function increased in 2004, up \$2.7 million.

Economic environment expenses decreased by \$6.7 million. Block grant spending decreased by \$3.8 million in 2004 due to the delay in some Office of Economic Development and Office of Housing projects. As a result of some staff reductions and the elimination of the Neighborhood Leadership Program and the Seattle Neighborhood Group, the Department of Neighborhood's costs were down \$1.2 million. Low-Income Housing Fund expenditures were also down. The reduction in spending of \$2.6 million reflects the year-to-year fluctuations in the spending patterns inherent to the programs funded by the Investment Partnership Program grants.

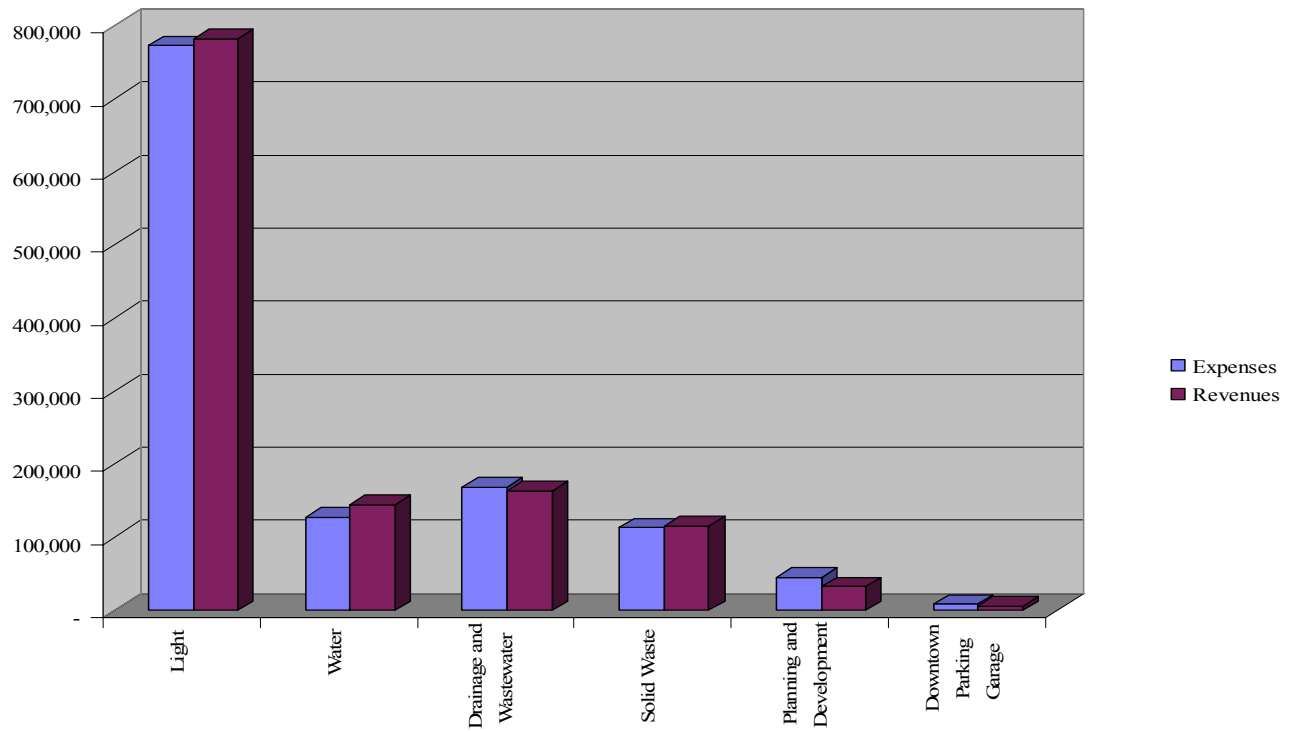
Health and human services expenses declined by \$1.3 million. The City's payments to King County for its share of health care costs went down in 2004.

At \$195.7 million, culture and recreation expenses were up \$31.2 million in 2004, an increase of 18.9 percent. In 2004 the construction of the new Central Library was completed, some new branch libraries were built, and older libraries were refurbished. Over \$10 million was expended for purchase of library materials, minor equipment, and supplies related to these various libraries. Depreciation expense increased \$5.1 million in 2004 as the City recently completed and placed several new buildings, including the Central Library and the McCaw Hall, into service. Workers' compensation and judgment and claims costs also increased significantly compared to 2003, up \$7.7 million. The Parks Department and Seattle Center also contributed to the increase.

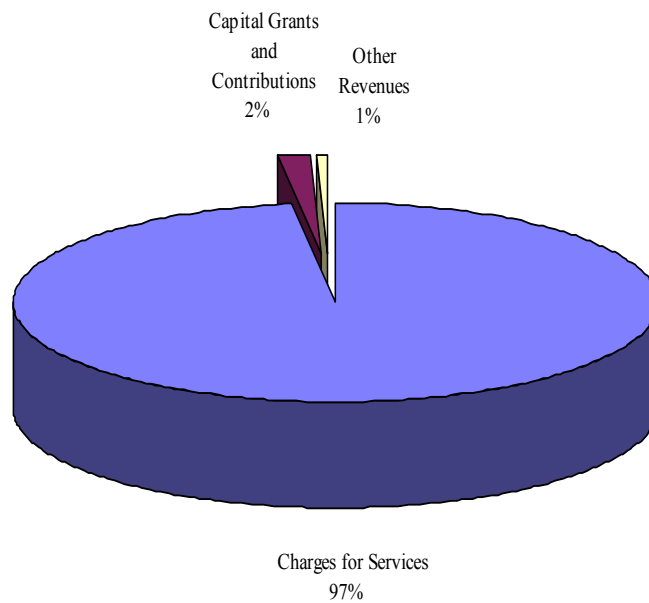
Interest on long-term debt went down by \$1.7 million or 4.0 percent as a result of a decrease in general obligation debt.

Business-Type Activities

EXPENSES AND PROGRAM REVENUES - BUSINESS-TYPE ACTIVITIES



REVENUES BY SOURCE - BUSINESS-TYPE ACTIVITIES



Total \$1,251.0 Million

Management's Discussion and Analysis

Business-Type Activities. Business-type activities increased the City's net assets by \$24.7 million to \$846.4 million, an increase of 3.0 percent. Key factors for the change are as follows:

The City Light Utility realized a net increase of \$13.8 million in net assets in 2004, an improvement of \$21.9 million from the net loss of \$8.1 million in 2003. Higher revenues from the sale of energy to retail customers account for most of the improvement in financial results. In 2004 City Light amortized the remaining power cost deferred from 2001. If power costs had not been deferred from 2001 and amortized over the 2002 - 2004 period, new income in 2004 would have been considerably higher.

The Water Utility experienced a net increase of \$17.8 million in net assets in 2004. This increase was primarily due to the rate increase effective January 1, 2004. Water consumption in 2004 was similar to that of 2003.

The Drainage and Wastewater Utility experienced a decrease of \$5.0 million in net assets in 2004. This decrease was largely due to the rise of expenses, such as operating expenses, depreciation, taxes, and interest due to a lesser amount of interest capitalized for construction projects.

The Solid Waste Utility net assets increased \$3.5 million in 2004 due primarily to a modest increase in operating revenues and grants received from the State of Washington to support SPU's Sustainable Buildings, Commercial Waste Reduction, Back Composting, and Illegal Dumping programs. In addition, certain expenses decreased, such as general and administrative, consultant costs, claims, information technology, and depreciation.

The Planning and Development Fund net assets decreased by \$2.6 million. The Downtown Parking Garage Fund experienced a decrease of \$2.2 million in net assets.

FINANCIAL ANALYSIS OF CITY FUNDS

As noted earlier, the City uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

Table A-3 REVENUE, EXPENDITURE, AND FUND BALANCE SUMMARY
GOVERNMENTAL FUNDS
(In Thousands)

	Major Funds			
	General Fund		Low-Income Housing Fund	
	2004	2003	2004	2003
Revenues				
Taxes	\$ 586,516	\$ 562,426	\$ 11,770	\$ 11,766
Licenses and Permits	13,752	15,955	-	1
Grants, Shared Revenues, and Contributions	22,278	16,624	6,175	4,882
Charges for Services	50,230	51,035	23	230
Fines and Forfeits	18,135	17,164	-	-
Parking Fees and Space Rent	26,847	27,328	32	31
Program Income, Interest, and Miscellaneous Revenues	12,832	17,056	9,551	5,994
Total Revenues	730,590	707,588	27,551	22,904
Expenditures	509,386	496,349	18,876	21,457
Other Financing Sources and Uses				
Long-Term Debt	-	-	-	-
Sales of Capital Assets	1,922	5,682	-	107
Transfers In (Out)	(209,769)	(207,465)	-	-
Total Other Financing Sources and Uses	(207,847)	(201,783)	-	107
Fund Balances				
Reserves Legally Segregated for Future Use	69,867	58,669	32,628	35,577
Reserves Not Available for Appropriation	21,640	17,921	-	-
Unreserved	40,669	42,228	14,004	2,381
Total Fund Balances	\$ 132,176	\$ 118,818	\$ 46,632	\$ 37,958

Table A-3 REVENUE, EXPENDITURE, AND FUND BALANCE SUMMARY
GOVERNMENTAL FUNDS (continued)
(In Thousands)

	Nonmajor Funds			
	Special Revenue Funds		Debt Service Funds	
	2004	2003	2004	2003
Revenues				
Taxes	\$ 33,466	\$ 32,655	\$ 25,765	\$ 27,756
Licenses and Permits	5,276	1,545	-	-
Grants, Shared Revenues, and Contributions	79,878	61,147	22	34
Charges for Services	62,437	60,244	-	-
Fines and Forfeits	2,660	2,334	-	-
Parking Fees and Space Rent	17,507	16,504	5,085	4,134
Program Income, Interest, and Miscellaneous Revenues	4,653	6,227	3,322	1,877
Total Revenues	205,877	180,656	34,194	33,801
Expenditures	367,292	375,922	94,175	90,712
Other Financing Sources and Uses				
Long-Term Debt	-	2,666	3,294	143
Sales of Capital Assets	652	1,076	-	-
Transfers In (Out)	152,084	173,389	58,652	57,319
Total Other Financing Sources and Uses	152,736	177,131	61,946	57,462
Fund Balances				
Reserves Legally Segregated for Future Use	24,922	19,548	14,935	12,970
Reserves Not Available for Appropriation	9,159	19,394	-	-
Unreserved	4,387	8,205	-	-
Total Fund Balances	\$ 38,468	\$ 47,147	\$ 14,935	\$ 12,970

	Nonmajor Funds				Total Governmental Funds	
	Capital Projects Funds		Permanent Funds		2004	2003
	2004	2003	2004	2003		
Revenues						
Taxes	\$ 57,526	\$ 32,436	\$ -	\$ -	\$ 715,043	\$ 667,039
Licenses and Permits	-	-	-	-	19,028	17,501
Grants, Shared Revenues, and Contributions	9,009	14,648	-	-	117,362	97,335
Charges for Services	-	228	-	-	112,690	111,737
Fines and Forfeits	-	-	-	-	20,795	19,498
Parking Fees and Space Rent	77	121	-	-	49,548	48,118
Program Income, Interest, and Miscellaneous Revenues	2,105	4,981	34	49	32,497	36,184
Total Revenues	68,717	52,414	34	49	1,066,963	997,412
Expenditures	119,499	222,833	154	500	1,109,382	1,207,773
Other Financing Sources and Uses						
Long-Term Debt	-	59,420	-	-	3,294	62,229
Sales of Capital Assets	406	-	-	-	2,980	6,865
Transfers In (Out)	(12,097)	(37,832)	(15)	(15)	(11,145)	(14,604)
Total Other Financing Sources and Uses	(11,691)	21,588	(15)	(15)	(4,871)	54,490
Fund Balances						
Reserves Legally Segregated for Future Use	101,296	110,928	31	12	243,679	237,704
Reserves Not Available for Appropriation	-	49,704	2,205	2,217	33,004	89,236
Unreserved	(3,137)	-	19	161	55,942	52,975
Total Fund Balances	\$ 98,159	\$ 160,632	\$ 2,255	\$ 2,390	\$ 332,625	\$ 379,915

Governmental Funds

The focus of the City's governmental funds is to provide information on near-term inflows, outflows, and balances of resources available for spending. This information is useful in assessing the City's financing requirements. In particular, unreserved fund balance measures the City's net resources available for spending at the end of the fiscal year. Governmental funds reported by the City include the General Fund, special revenue funds, debt service funds, capital project funds, and permanent funds.

As of the end of the current fiscal year the City's governmental funds reported combined ending fund balances of \$332.6 million, a decrease of \$47.3 million in comparison to 2003. Approximately \$56.0 million of this amount constitutes unreserved fund balance which is available for spending at the City's discretion within the purposes specified for the City's funds. The remainder of fund balance is reserved to indicate that it is not available for new spending because it has been committed for other purposes such as (1) payment on existing contracts and purchase orders, \$40.1 million; (2) funding of continuing projects and programs in future periods, \$172.5 million; (3) payment of debt service, \$27.7 million; and (4) a variety of other purposes, \$36.3 million.

Revenues for governmental funds overall totaled approximately \$1.067 billion in the fiscal year ended December 31, 2004, which represents an increase of approximately 7.0 percent from the prior fiscal year. Expenditures in governmental funds amounted to \$1.109 billion, a decrease of approximately 8.1 percent during the same period. In the aggregate, expenditures for governmental funds exceeded revenues by approximately \$42.4 million.

The **General Fund** is the chief operating fund of the City. It is composed of sixteen subfunds: General, Judgment/Claims, Arts Account, Cable Television Franchise, Cumulative Reserve, Neighborhood Matching, City Hall, Development Rights, Police Support Facility, Emergency, Street Vacation Compensation, Special Employment Program, Industrial Insurance, Unemployment Compensation, Health Care, and Group Term Life Insurance. Table A-4 provides a summary of the status of the various subfunds at year-end 2004.

At the end of 2004 the total fund balance of the General Fund was \$132.2 million. Fund balance increased by \$13.4 million in 2004 compared to 2003.

Total revenues for the General Fund increased \$23.0 million, 3.3 percent higher than 2003. Tax revenues increased by \$24.1 million, an indicator of the economic recovery from the 2001 recession. The City Council approved a one-percent rate increase in property taxes for 2004 while robust activity in new construction and other homes sales contributed to an increase in real estate excise tax revenues. Sales tax revenues and B&O tax increases also contributed to the increase in total tax revenues.

Revenue from licenses and permits decreased by \$2.2 million. In 2004, while the new police alarm licensing fee brought in \$1.5 million, it was offset by a reduction in revenue from the move of street permit revenue (approximately \$2.7 million) to the Transportation Fund as well as a decrease in revenue of \$0.7 million in business license renewals. Due to a late change in the fee structure the penalty deadline for business license renewals was extended until February 1, 2005. Revenue from grants, shared revenues, and contributions increased by \$5.7 million. The majority of the increase was related to the Urban Areas Security Initiative (UASI) grant from the Department of Homeland Security. On the other hand, revenue from program income, interest, and miscellaneous revenue decreased \$4.2 million mostly due to declining investment earnings.

General Fund expenditures increased by \$13.0 million or 2.6 percent in 2004, from \$496.4 million to \$509.4 million. With the receipt of the UASI grant from the Department of Homeland Security, spending by the Police Department and the Fire Department on emergency preparedness and training increased. Both departments also incurred additional costs to provide security for the Monorail and Sound Transit construction projects. As a result of the Okeson streetlight lawsuit, in 2004 the General Fund began paying the \$6.2 million annual operating costs of the City's streetlights as well as an additional \$6.0 million in 2004 towards prior years' costs that are being refunded to rate payers. To offset some of the streetlight impact, the budgets of the general government departments were reduced in 2004. The spending for claims and lawsuits was also down in 2004 and the General Fund incurred a one-time cost of \$10.8 million for property for a Joint Training facility in 2003 whereas no comparable purchase was recorded in 2004.

Changes in the other financing sources and uses category reduced the General Fund's fund balance position in 2004. In 2003 net interfund transfers out of the General Fund to support other City Funds' activities were \$207.5 million. In 2004 net transfers out increased slightly to \$209.8 million. In 2003 the General Fund received \$5.7 million from the sale of capital assets. In 2004 the amount received was only \$1.9 million.

The **Low-Income Housing Fund**, a special revenue fund and one of the major governmental funds of the City, manages activities undertaken by the City to preserve, rehabilitate, or replace low-income housing. It also accounts for the seven-year housing levy approved by voters in 1995. An additional seven-year levy was approved by the voters in November 2002. At \$46.6 million, the Low-Income Housing Fund ended the year with a fund balance increase of \$8.7 million. Revenue increased by \$4.7 million compared to 2003. In 2004 the Low-Income Housing Fund received \$4.3 million proceeds from the sale of development rights to Washington Mutual, and grant revenues increased by \$1.3 million. These revenue

increases were offset by a decrease in investment earnings of \$1.3 million as a result of declining interest rates. Expenditures in 2004 were \$2.6 million lower than 2003. The decline is attributed to the Home Investment Partnership program.

In 2004 the other **special revenue funds** showed an \$8.7 million or 18.4 percent decrease in fund balance as a result of operations. The most significant changes occurred in the Education and Development Services Fund (\$9.1 million), Seattle Center Fund (\$2.5 million), Transportation Fund (\$1.3 million), Park and Recreation Fund (\$1.2 million), and the Municipal Arts Fund (\$1.1 million). On the positive side, the Library Fund increased by \$6.5 million. In the 2004 adopted budget the City planned to use the balances of various City funds on a one-time basis. These balances reflected past cost savings, revenues over-performance, or use of reserves.

Total revenues for the other special revenue funds were up \$25.2 million, 14.0 percent. Grants and contributions accounted for the majority of the increase, up \$18.7 million. The Library Fund recorded \$28.0 million in grants and contributions in 2004. Private donations from the Library Foundation accounted for the bulk of the increase. Taxes increased slightly up by \$0.8 million. Licenses and permits increased by \$3.7 million. In 2004 revenue from street permits was moved from the General Fund to the Transportation Fund, accounting for the majority of the increase. Charges for services went up by \$2.2 million and parking fees and space rent by \$1.0 million. Program income, interest and miscellaneous revenues declined by \$1.6 million.

Expenditures decreased by \$8.6 million, a 2.3 percent decline. In 2003 a one-time expenditure of \$20.0 million was incurred for a loan to the monorail project. The Library Fund spent \$11.4 million more in 2004 compared to 2003. The increase was due to spending on construction and improvements at various libraries as well as the purchase of additional books and materials and the increased cost to operate the new and expanded libraries. Although there are increases in expenditures for the Parks and Recreation Fund (\$3.5 million), Education and Development Services Fund (\$1.5 million), and Seattle Center (\$1.0 million), these were mostly offset by the decrease in spending for the Housing and Community Revenue Sharing Fund (\$3.8 million) and the Transportation Fund (\$1.0 million).

The Other Financing Sources and Uses category decreased by \$24.4 million in 2004, a 13.8 percent reduction from 2003. The two main reasons for the decrease are: (1) a \$20.5 million reduction in operating support from the General Fund due to both the planned spend-down of fund balances and budget cuts related to the Okeson streetlight litigation and (2) a \$2.6 million decrease in long-term debt issues related to draws from the Washington State Public Works Trust Loan made in 2003.

The fund balance in the **capital projects funds** continued to decline in 2004 as a result of construction activity, down \$62.5 million or 38.9 percent to \$98.2 million. The Libraries for All Fund and the Municipal Civic Center Fund accounted for the majority of the decline, down \$23.6 million and \$18.2 million respectively. In addition, the 2003 Long-Term General Obligation Project, Seattle Center and Parks Multipurpose Levy Fund, and the 2002B Long-Term General Obligation project accounted for \$9.6 million, \$6.9 million and \$6.7 million, respectively, while the Public Safety Technology Fund ended on a positive note with an increase of \$7.7 million.

Revenues for the capital projects funds were \$68.7 million in 2004. This is \$16.3 million or 31.1 percent higher than 2003 revenues. The increase is due to the new 2003 fire facilities levy approved by the voters in November 2003. The tax levy proceeds are being deposited into the Public Safety Information Technology Fund.

Expenditures for capital projects were \$119.5 million in 2004, a decrease of \$103.3 million or nearly half (46.4 percent) of the total expended in 2003. Several major projects were completed or nearly complete at the end of 2003. The City's opera house, the Marion Mc Caw Hall, opened in June 2003. Work on the new Central Library continued in 2003, and the Library opened in May 2004. The City's new Civic Center neared completion with the opening of City Hall in the summer of 2003. The City Hall Plaza was completed in early 2005.

The **debt service funds** showed an increase in fund balance of \$2.0 million, up 15.2 percent in 2004. The increase is attributed to an insurance recovery of \$1.8 million related to the 2001 earthquake plus interest earnings recognized in 2004. The **permanent funds** showed a balance of \$2.3 million at year-end, a minor decrease of \$0.1 million compared to 2003.

Management's Discussion and Analysis

Table A-4 **REVENUE, EXPENDITURE, AND FUND BALANCE SUMMARY**
GENERAL FUND SUBFUNDS
(In Thousands)

	<u>General</u>	<u>Judgment/ Claims</u>	<u>Arts Account</u>	<u>Cable Television Franchise</u>	<u>Cumulative Reserve</u>	<u>Neighborhood Matching</u>
Revenues						
Taxes	\$ 547,855	\$ -	\$ -	\$ -	\$ 38,661	\$ -
Licenses and Permits	11,267	-	-	2,485	-	-
Grants, Shared Revenues, and Contributions	20,736	-	-	-	1,542	-
Charges for Services	39,428	10,217	-	-	2	-
Fines and Forfeits	18,132	3	-	-	-	-
Parking Fees and Space Rent	11,870	-	-	-	220	-
Program Income, Interest, and Miscellaneous Revenues	1,899	47	-	632	(1,185)	-
Total Revenues	<u>651,187</u>	<u>10,267</u>	<u>-</u>	<u>3,117</u>	<u>39,240</u>	<u>-</u>
Expenditures	466,029	5,432	-	-	14,908	3,728
Other Financing Sources and Uses						
Sales of Capital Assets	5	-	-	-	1,121	-
Transfers In (Out)	(173,872)	(1,199)	(248)	(3,253)	(19,007)	3,088
Total Other Financing Sources and Uses	<u>(173,867)</u>	<u>(1,199)</u>	<u>(248)</u>	<u>(3,253)</u>	<u>(17,886)</u>	<u>3,088</u>
Fund Balances						
Reserves Legally Segregated for Future Use	11,260	12,783	-	-	38,044	4,419
Reserves Not Available for Appropriation	2,688	-	-	-	-	-
Unreserved	19,588	-	-	1,465	(4,672)	897
Total Fund Balances	<u>\$ 33,536</u>	<u>\$ 12,783</u>	<u>\$ -</u>	<u>\$ 1,465</u>	<u>\$ 33,372</u>	<u>\$ 5,316</u>

	<u>City Hall</u>	<u>Development Rights</u>	<u>Police Support Facility</u>	<u>Emergency</u>	<u>Street Vacation Compensation</u>	<u>Special Employment Program</u>
Revenues						
Taxes	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Licenses and Permits	-	-	-	-	-	-
Grants, Shared Revenues, and Contributions	-	-	-	-	-	-
Charges for Services	-	-	-	-	-	305
Fines and Forfeits	-	-	-	-	-	-
Parking Fees and Space Rent	13,150	-	1,607	-	-	-
Program Income, Interest, and Miscellaneous Revenues	-	180	-	(113)	-	-
Total Revenues	<u>13,150</u>	<u>180</u>	<u>1,607</u>	<u>(113)</u>	<u>-</u>	<u>305</u>
Expenditures	10,802	-	1,521	46	-	1,448
Other Financing Sources and Uses						
Sales of Capital Assets	-	-	-	-	794	-
Transfers In (Out)	(13,948)	(841)	(1,656)	1,505	(600)	-
Total Other Financing Sources and Uses	<u>(13,948)</u>	<u>(841)</u>	<u>(1,656)</u>	<u>1,505</u>	<u>194</u>	<u>-</u>
Fund Balances						
Reserves Legally Segregated for Future Use	-	-	-	47	28	-
Reserves Not Available for Appropriation	-	-	-	18,952	-	-
Unreserved	(2,306)	(661)	(61)	12,729	-	104
Total Fund Balances	<u>\$ (2,306)</u>	<u>\$ (661)</u>	<u>\$ (61)</u>	<u>\$ 31,728</u>	<u>\$ 28</u>	<u>\$ 104</u>

Table A-4 REVENUE, EXPENDITURE, AND FUND BALANCE SUMMARY
GENERAL FUND SUBFUNDS (continued)
(In Thousands)

	Industrial Insurance	Unemployment Compensation	Health Care	Group Term Life Insurance	Total General Fund	
					2004	2003
Revenues						
Taxes	\$ -	\$ -	\$ -	\$ -	\$ 586,516	\$ 562,426
Licenses and Permits	-	-	-	-	13,752	15,955
Grants, Shared Revenues, and Contributions	-	-	-	-	22,278	16,624
Charges for Services	278	-	-	-	50,230	51,035
Fines and Forfeits	-	-	-	-	18,135	17,164
Parking Fees and Space Rent	-	-	-	-	26,847	27,328
Program Income, Interest, and Miscellaneous Revenues	-	1,714	9,658	-	12,832	17,056
Total Revenues	278	1,714	9,658	-	730,590	707,588
Expenditures	433	-	4,667	372	509,386	496,349
Other Financing Sources and Uses						
Sales of Capital Assets	2	-	-	-	1,922	5,682
Transfers In (Out)	-	-	262	-	(209,769)	(207,465)
Total Other Financing Sources and Uses	2	-	262	-	(207,847)	(201,783)
Fund Balances						
Reserves Legally Segregated for Future Use	5	-	3,281	-	69,867	58,669
Reserves Not Available for Appropriation	-	-	-	-	21,640	17,921
Unreserved	4,745	2,193	6,648	-	40,669	42,228
Total Fund Balances	\$ 4,750	\$ 2,193	\$ 9,929	\$ -	\$ 132,176	\$ 118,818

Proprietary Funds

The City's proprietary funds provide the same type of information found in the government-wide financial statements but in more detail.

City Light Utility. The Utility realized net income of \$13.8 million in 2004 compared to a net loss of \$8.1 million in 2003. Revenue from sales of energy to retail customers accounts for the majority of the increase. Retail revenue was up \$24.5 million compared to 2003. At \$113.6 million, revenue from wholesale power sales (net of cost of wholesale purchases) remained fairly constant compared to the prior year. Lower power costs, in particular a reduction of \$26.1 million in the cost of power purchased from the Bonneville Power Administration, were partially offset by a slight increase in other operations and maintenance costs. Income from fees and grants were \$8.3 million lower than in 2003.

City Light incurred a net loss of \$73.3 million during the energy crisis of 2001 after deferral of \$300.0 million in excess power costs from 2001 to future years pursuant to SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*, and City of Seattle Ordinance No. 120385. In December 2004 the Utility amortized the final monthly installment of \$8.3 million. Without the deferral and amortization of power costs in 2004, net income would have been \$113.8 million.

Net cash provided by operating activities increased to \$242.2 million in 2004, compared to \$214.9 million in 2003, an increase of \$27.3 million. Restricted cash and investments were \$123.7 million in 2004, down from \$159.4 million in 2003. The decrease was largely due to the reduction in the amount of bond proceeds remaining at year-end. Operating cash balances at year-end increased from \$9.3 million in 2003 to \$60.7 million in 2004 reflecting positive cash flow from operations, net of the repayment of \$70 million in interdepartmental operating debt.

Utility plant and other capital assets were \$1.408 billion and \$1.391 billion in 2004 and 2003, respectively, a net increase of \$17 million. The majority of the capital asset additions were in the distribution system.

City Light issued \$284.9 million new improvement and revenue refunding bonds in 2004. \$215.3 million revenue bond proceeds were used to defease certain 1995A, 1996 and 1999 bonds. The remaining amount was used for construction and acquisition of capital and deferred assets. Total net revenue bonds payable were \$1.537 billion in 2004 and \$1.522 billion in 2003, a net increase of \$15.7 million. Interest expenses were \$73.8 million in 2004 and \$73.9 million in 2003. Debt service coverage ratios were 1.58 in 2004 and 1.56 in 2003. Including long-term debt, the total liabilities were \$1.722 billion in 2004 and \$1.770 billion in 2003.

Total net assets were \$303.9 million in 2004 and \$290.1 million in 2003.

Water Utility. Operating income of the Water Utility increased to \$40.3 million in 2004 from \$34.9 million in 2003. Net income rose slightly to \$17.8 million in 2004 from \$16.9 million in 2003, an increase of \$0.9 million. The net income increase was primarily due to a rate increase and contributions from developers and other local governments for infrastructure projects, offset by the absence of a significant one-time gain in 2004 (\$6.8 million for the sale of a power transmission right-of-way easement to the Bonneville Power Administration received in 2003).

Net cash provided by operating activities rose to \$74.3 million in 2004 from \$72.2 million in 2003, an increase of \$2.1 million. Total operating and restricted cash and investments were \$124.8 million in 2004 compared to \$73.2 million in 2003, an increase of \$51.6 million. This increase in cash and investments resulted from proceeds of the sale of revenue bonds and deposits made into the revenue stabilization fund.

Utility plant and other capital assets were \$969.2 million and \$933.1 million in 2004 and 2003, respectively, an increase of \$36.1 million. Significant capital was spent on the construction of the new Cedar River water treatment facility and on pipeline, conservation, and distribution system improvements.

The Water Utility issued \$84.8 million in revenue bonds to finance the water system capital program. Total revenue bonds payable was \$794.6 million and \$731.5 million in 2004 and 2003, respectively. Interest expenses were \$29.4 million in 2004 and \$27.3 million in 2003. Bond covenants require net revenues for debt service at 125 percent for both 2004 and 2003, while actual net revenues for debt service were 169 percent for 2004 and 164 percent for 2003. Including revenue bonds payable, total liabilities were \$847.1 million and \$775.9 million in 2004 and 2003, respectively.

Total net assets were \$298.3 million in 2004 and \$280.5 million in 2003.

Drainage and Wastewater Utility. Operating income of the Utility increased to \$9.1 million in 2004 from \$7.4 million in 2003, a net increase of \$1.7 million. Operating revenues increased \$11.4 million and operating expenses increased \$9.7 million between 2004 and 2003. The Utility incurred a net loss of \$5.0 million in 2004 and \$4.3 million in 2003. This loss was caused primarily by increases in environmental charges and interest expenses.

Net cash provided by operating activities increased to \$19.7 million in 2004 from \$16.9 million in 2003. Total operating and restricted cash and investments were \$64.2 million in 2004 compared to \$26.0 million in 2003, an increase of \$38.2 million. This increase in cash and investments was associated with proceeds from the sale of revenue bonds.

Utility plant and other capital assets increased to \$475.7 million in 2004 from \$460.9 million in 2003, an increase of \$14.8 million. Significant investments in capital assets were for improvements to the wastewater collection and conveyance system, improvements to the drainage collection and conveyance system, and habitat projects.

The Utility issued \$62.0 million in revenue bonds to finance additions and improvements to the drainage and wastewater system. The total outstanding bond liabilities were \$301.2 million in 2004 and \$244.4 million in 2003, an increase of \$56.8 million. Interest expenses were \$10.8 million in 2004 and \$9.4 million in 2003. Debt service coverage ratio requirements were 125 percent for both 2004 and 2003, and actual debt service coverage ratios were 219 percent in 2004 and 212 percent in 2003. Total liabilities, including revenue bonds, were \$336.8 million in 2004 and \$271.8 million in 2003.

Total net assets were \$243.2 million in 2004 and \$248.2 million in 2003.

Fiduciary Funds

The City maintains fiduciary funds for the assets of the City of Seattle Employees' Retirement System (SCERS), the Firemen's Pension Fund, the Police Relief and Pension Fund, the S.L. Denny Private Purpose Trust Fund, and various agency funds. Total net assets of the combined fiduciary funds at the end of 2004 were \$1.692 billion. SCERS represents 99.5 percent of that amount.

SCERS assets that are held in trust for the payment of future benefits exceeded its current amounts owed as of December 31, 2004 by \$1.684 billion. Net assets increased by \$157.0 million during 2004, primarily due to gains in the equity markets in the U.S. and abroad. Total revenues (additions to net assets) for 2004 were \$245.8 million, which includes member and employer contributions of \$74.0 million and net investment income totaling \$171.8 million. In 2004 total expenses (deductions to net assets) were \$88.8 million. While payments for retiree benefits increased by \$3.7 million, this increase was offset largely by fewer refunds of contributions, resulting in a slight increase in total expenses of just \$0.2 million compared to 2003.

At December 31, 2004 the net assets held in trust in the Firemen's Pension Fund and the Police Relief and Pension Fund for the payment of future benefits were \$6.2 million and \$1.8 million respectively.

GENERAL FUND BUDGETARY HIGHLIGHTS

The City's final expenditure budget for the General Fund differed from the original budget due to supplemental legislation/appropriations approved during the year. In fiscal year 2004 the General Fund's original budget was \$676.8 million. That original budget was increased by \$22.2 million (3.2 percent) in supplemental appropriations after a reduction for reimbursements received for Personnel's services (a \$98.6 million reduction for reimbursements).

The most significant budget revisions are described below:

- In November 2003, at about the time of the completion of the 2004 Budget, the State Supreme Court ruled that the City's practice of having the Light Fund pay for streetlights was unconstitutional and that these costs were the responsibility of the General Fund. In February 2004 the Mayor and various members of the City Council worked to explore options to address the streetlight funding issue as well as to prepare for upcoming 2005 budget pressures. The resulting ordinance, 121430, reduced the General Fund budget, including support to other funds, by a \$7.7 million. All General Fund supported-departments were impacted by the budget cut. Later, ordinance 121556 appropriated \$6.2 million to cover the 2004 estimated costs for streetlights.
- The City Council authorizes the acceptance of all grant funds. If a grant is not included as a part of the adopted budget, a separate ordinance is required. In 2004 over \$22 million in additional grant funds were appropriated. Most of the grant funds were for public safety purposes including over \$16 million in UASI/Homeland Security grants to increase the capacity of the Seattle urban area to prevent, respond to, and recover from threats or acts of terrorism.
- Funds were also appropriated during 2004 for earthquake repair. The funding is for damages resulting from the 2001 Nisqually earthquake. Many City facilities were damaged during the quake, and repair work continues.

At year-end 2004 actual expenditures were \$87.3 million less than budgeted. Of this amount, \$52.1 million of the budget was carried over into 2005 to cover outstanding encumbrances, grants, capital spending, and special carryovers. The balance of the expenditure budget, \$35.1 million, was lapsed. The Health Care Subfund contributed \$14.6 million to the underspending of budget in the General Fund because actual costs for employees' medical and dental coverage were significantly less than the budgeted amount. With a lapse amount of \$6.9 million, costs for the Special Employment Subfund were also significantly under budget. The Police Department was the only other department to lapse any significant budget, \$5.1 million.

During the year budgetary revenue estimates exceeded actual revenues by \$14 million. While tax revenues exceeded the budget by \$23.9 million, and fines and forfeits were \$2.3 million greater than budget, revenue from all other categories were less than budget. Of this amount, \$4.4 million is attributable to lower than anticipated space rental and parking fees, \$7.4 million is due to lower Special Employment Fund fees, and \$14.5 million is from reduced health care premiums. An additional \$10.0 million is related to incomplete grant projects and is expected to be collected in the future.

CAPITAL ASSETS

The following schedule shows the City's investment in capital assets.

Table A-5 CAPITAL ASSETS AT YEAR END, NET OF DEPRECIATION
(In Thousands)

	Governmental Activities		Business-Type Activities		Total	
	2004	Restated 2003	2004	2003	2004	Restated 2003
Land	\$ 364,094	\$ 345,578	\$ 64,885	\$ 62,597	\$ 428,979	\$ 408,175
Plant in Service, Excluding Land	-	-	2,577,802	2,385,280	2,577,802	2,385,280
Buildings and Improvements	1,256,563	1,003,846	58,410	60,844	1,314,973	1,064,690
Machinery and Equipment	85,353	82,099	7,467	8,475	92,820	90,574
Infrastructure	459,465	460,482	-	-	459,465	460,482
Construction in Progress	212,524	362,436	221,767	350,041	434,291	712,477
Other Capital Assets	7,607	6,369	15,117	14,510	22,724	20,879
Total Capital Assets	\$ 2,385,606	\$ 2,260,810	\$ 2,945,448	\$ 2,881,747	\$ 5,331,054	\$ 5,142,557

Capital assets for governmental activities increased \$124.8 million in 2004. Major increases include the following:

- Seattle Center completed construction of the Marion Oliver McCaw Hall in 2003. An additional \$2.3 million in construction costs were capitalized in 2004. Seattle Center also capitalized \$3.7 million for various other improvements.
- The Fleets and Facilities Department (FFD) purchased land at a cost of \$10.4 million with funds from the new 2003 fire levy for an emergency/fire alarm center. FFD completed construction of the new City Hall in 2003. Additional costs of \$1.2 were capitalized in 2004 as were \$24.6 million in other improvements. Over 70 percent of the improvement costs were for the Park 90/5 complex, which opened in mid-2004.
- The Parks Department completed construction work on the Yesler Community Center, the Sand Point Community Center, the High Point Community Center, the Jefferson Park Community Center expansion, the International Community Center, and the Southwest Community Center gym at a total cost of \$20.5 million. The Department also completed numerous parks improvements at a cost of \$53.1 million and purchased a few parcels of land for a total of \$2.5 million.
- The Transportation Department capitalized \$24.3 million for various infrastructure assets (roads, bridges, sidewalks, signs, signals, illuminations, and others) and \$0.1 million for land acquisition. Construction in progress increased by \$17.3 million.
- The Library completed construction of the new Central Library at a cost of \$152.6 million. The library opened in May 2004. The Library also completed construction work at several branch libraries, such as the Beacon Hill Library, the Northeast Library, the Rainier Beach Library, and the Columbia Library, spending an additional \$26.7 million. Construction in progress at December 31, 2004, was \$42.5 million.

Capital assets for business-type activities increased \$63.7 million, as follows:

- City Light capital assets increased by approximately \$17.3 million. These increases were mainly for improvements to the hydroelectric system, transmission plant, and distribution plant as well as for land and land rights. The hydroelectric system improvements were for the completion of the North Cascades Environmental Learning Center, upgrading exhibits at Newhalen, the Boundary rehabilitation project, improvement of Gorge Road, and other work. The transmission plant increases were mainly for circuit breaker replacements at substation switch yards. The distribution plant increases were for poles, overhead conductors for capacity additions and relocations, underground conduits, Broad Street substation network, Sound Transit, overhead and underground services meter additions, and streetlights.
- Water Utility capital assets increased \$37.6 million. Major capital outlays were for the completion of the Cedar River Treatment Facility, numerous computer hardware and software application upgrades, installation of new direct service meters and replacement meters, and improvements to the distribution of water mains.
- Drainage and Wastewater Utility capital assets increased \$11.6 million. Major capital improvements included the completion of Phase II of the Jackson Park Detention Pond, completion of the natural drainage system at 3rd and 107th Streets, completion of Phase II of the Delridge Basin, rehabilitation of sewer pipes, storm drain improvements, and rehabilitation of 5 pump stations.
- Nonmajor funds capital assets decreased \$2.8 million, largely due to depreciation.

More detail about the City's capital assets is presented in Note 5 to the financial statements.

DEBT ADMINISTRATION

At the end of the 2004 fiscal year the City had \$3.574 billion in outstanding bonded debt, compared to \$3.492 billion in 2003. This represents an increase of approximately \$82.0 million (2.3 percent).

In 2004 the City issued revenue bonds to finance various capital improvement projects, additions and conservation programs of the City's Light, Water and Drainage and Wastewater systems. Additional revenue anticipation notes were issued to finance ongoing capital projects for the Solid Waste Utility. To take advantage of the low-interest rates and improve cash flow, the City refinanced a general obligation bond issue and three series of revenue bonds for a total of \$305.1 million. By refinancing the debt the City will save \$29.7 million in principal and interest over the next 15 to 20 years. Additionally, the City defeased \$4.3 million of the 1994 Coliseum bonds, placing its own resources into an irrevocable trust to service the debt when it is due or called.

The City's unlimited tax general obligation bonds are rated Aaa by Moody's Investors Service, AAA by FitchRatings, and AAA by Standard & Poors. The City's limited tax general obligation bonds are rated Aa-1 by Moody's Investors Services, AA+ by FitchRatings, and AAA by Standard & Poors. The City maintained its high bond ratings on its Light, Water, Drainage and Wastewater, and Solid Waste revenue bonds. The City's limited and unlimited general obligation debt is capped at 7.5 percent of assessed value by state law. The 2005 assessed value for the City is \$88.3 billion. At year-end

2004 the net outstanding general obligation debt of the City that includes bonds, leases, compensated absences net of sick leave, and guarantees of indebtedness amounted to \$978.5 million, well below the limit of \$6.6 billion. Within the 7.5 percent limitation, state law restricts outstanding limited tax general obligation bonds to 1.5 percent of assessed value. At year-end 2004 the net outstanding limited tax general obligation was \$686.1 million.

The City is self-insured for workers compensation and for most health care costs. The City carries general liability insurance with a self-insured retention. For these claims, including those incurred but not reported, the City recognized a total liability of \$102.0 million at end of the year. In addition, the City's utilities recorded \$14.9 million in estimated environmental liabilities. At the end of 2004 City Light had \$35.7 million in liabilities related to its purchased power commitments. Other obligations were accrued compensated absences and other notes and contracts. The other notes and contracts included draws from the State's Public Works Trust Loan Program which are serviced with revenues from two participating City departments, one a governmental-type fund and another whose activities are reported in two of its business-type funds.

More detailed information about the City's long-term liabilities is presented in Note 8 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET AND RATES

The Puget Sound region endured a difficult economic recession beginning in 2001. The region lost 6.7 percent of its jobs between December 2000 and September 2003. The regional recession led to declines in many City revenues, including sales taxes, business and occupation (B&O) taxes, electricity sales, and water revenues.

The revenue effects of the poor regional economy have been exacerbated by a variety of other challenges. Changes in state law since 2000 have reduced Seattle's potential 2005 General Fund revenues by more than \$45 million. The largest component of this is due to Initiative 747, which was approved by the state's voters in 2001 and limits annual property tax revenue growth to 1 percent plus the value of new construction versus the previous limit of 6 percent plus new construction..

Revenues available for transportation projects were adversely affected by Initiative 776, which was approved by the state's voters in 2002. This Initiative eliminated the vehicle license fee collected by King County and shared with cities. The loss of this revenue, coupled with continuing declines in the value of gasoline tax revenues to cities, has created a looming funding crisis for transportation in Seattle and other Washington cities.

The State Supreme Court's decision in the Okeson v. Seattle case was handed down in November 2003. The Court ruled the City's practice of having the Light Fund pay for streetlights was unconstitutional and these costs were the responsibility of the General Fund. The Okeson case was remanded to Superior Court for further consideration of various issues. Most significantly, the Superior Court ruled that the General Fund must reimburse the Light Fund for \$23.1 million of streetlight costs incurred between December 1999 and November 2003. In addition, the Superior Court ruled certain other costs charged to the Light Fund were inappropriate. The City has appealed the decision related to the 1% for Art program.

The City's 2005-2006 budget reflects the fiscal realities facing the City while continuing commitments to core services. The budget is guided by the four priorities of Mayor Greg Nickels: transportation, public safety, economic development, and strong families and healthy communities. Regional economic growth, more efficient delivery of services, reductions or eliminations of lower-priority functions, and a small increase in some utility taxes allow for more focus on these priorities in the 2005 adopted budget.

The Mayor and City Council are committed to creating a sustainable budget for the General Fund and other City funds, including the utilities. The 2005-2006 General Fund Budget makes minimal reliance on fund balances or other one-time revenue sources. Revenues from nonrecurring sources, such as property sales, are dedicated to one-time projects rather than ongoing expenditures. Under current economic assumptions, the 2006 budget should be sustainable in future years.

The 2005-2006 budget reflects changes in some utility rates needed to continue services and to add resources to high-priority programs. Electrical rates have not been changed, pending a comprehensive review of City Light financial policies, revenue requirements, cost allocations, and rate design in the first half of 2005.

About 136 general government full-time-equivalent positions were eliminated in the 2005 budget.

General Fund revenues are projected to grow at a rate of 4.6 percent. At 26.8 percent, property taxes continue to be the largest source of General Fund revenue. The property tax forecast assumes no major policy changes and is projected to increase by the annual 1 percent growth limit plus new construction. The retail sales tax is expected to contribute 17.7 percent of the total General Fund revenues. After several years of decline, the retail sales tax showed improvement in 2004 and is expected to grow more strongly in 2005. Similarly, an improved economy is expected to boost B&O tax revenue in 2005. Approximately 17.4 percent of General Fund revenue is expected to come from the B&O tax. In 2005 there will be large increases in the utility tax revenue for all City utilities except City Light. These increases result from the City Council's decision to raise the utility tax rate from 10.0 percent to 11.5 percent for water, drainage, wastewater, the City's

solid waste utility, and private garbage. In addition, the water utility tax is increased by an additional 4.0 percent to pay for the cost of shifting fire hydrant services from utility revenues to General Fund revenues. Customers will not be affected because the tax rate increase is offset by a decrease in water rates.

Financial Contact

The City's financial statements are designed to provide users with a general overview of the City's finances as well as to demonstrate the City's accountability to its citizens, investors, creditors, and other customers. If you have a question about the report, please contact the City of Seattle, Department of Executive Administration, Accounting Services Division, P.O. Box 94669, Seattle, WA 98124-4669 (Telephone 206-386-9124).